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IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

NORTHERN ILLINOIS GAS COMPANY,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

REPLY BRIEF FOR PETITIONER NORTHERN ILLINOIS GAS COMPANY

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TABLE OF CONTENTS

		PAGE
I.	The Questions Presented Affect Hundreds Of Pending Cases And Many Millions of Dollars In Tax Liability Are Involved	2
II.	The Seventh Circuit Has Seriously Misconstrued The Highway Use Tax Act	5
Conclusion		10

TABLE OF AUTHORITIES

Cases

	PAGE
Alabama Power Co. v. *United States*, ____ F. Supp. ____, 85-1 U.S.T.C. ¶ 16,432, No. 83-AR-3014-S (N.D. Ala. 1985)	3
Consolidated Edison Co. v. *United States*, ____ F. Supp. ____, 85-1 U.S.T.C. ¶ 16,431, No. 84 Civ. 1167 (S.D.N.Y. 1985), *appeal pending before the Second Circuit*	3
Corn Products Refining Co. v. *Commissioner*, 350 U.S. 46 (1955)	8
Ernst & Ernst v. *Hochfelder*, 425 U.S. 185 (1976)	6
Minnesota Power and Light Co. v. *United States*, 6 Cl. Ct. 558 (1984), *appeal pending before the Federal Circuit*	2
Northern States Power Co. v. *United States*, 663 F.2d 55 (8th Cir. 1981), *cert. denied*, 456 U.S. 965 (1982)	2
Pacific Gas & Electric Co. v. *United States*, 664 F.2d 1133 (9th Cir. 1981)	2
Taxation with Representation Fund v. *IRS*, 646 F.2d 666 (D.C. Cir. 1981)	7
United States v. *Chicago, Burlington & Quincy Railroad Co.*, 412 U.S. 401 (1973)	4, 5

Miscellaneous

Revenue Ruling 57-547, 1957-2 C.B. 789	6
Revenue Ruling 60-260, 1960-2 C.B. 347	6
Revenue Ruling 72-109, 1972-1 C.B. 351	6
Revenue Ruling 74-539, 1974-2 C.B. 376	6
Revenue Ruling 74-461, 1974-2 C.B. 377	6
Revenue Ruling 74-513, 1974-2 C.B. 377	6
Revenue Ruling 75-297, 1975-2 C.B. 443	6
Revenue Ruling 76-558, 1976-2 C.B. 360	6

	PAGE
Revenue Ruling 76-294, 1976-2 C.B. 364	5, 7, 8
Revenue Ruling 76-559, 1976-2 C.B. 365	6
Revenue Ruling 77-36, 1977-1 C.B. 347	6
Revenue Ruling 78-156, 1978-1 C.B. 365	6
Revenue Ruling 78-208, 1978-1 C.B. 366	6
Revenue Ruling 78-314, 1978-2 C.B. 269	6
General Counsel's Memorandum 38962, *CCH IRS Positions* ¶ 1164 (February 16, 1983)	7
General Counsel's Memorandum 30742 (June 19, 1958)	6

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The United States contends that this case lacks sufficient practical importance to justify certiorari despite the fact that three Circuits and numerous district courts have divided on the legal questions presented, despite the fact that appeals are now pending in two additional Circuits, and despite the fact that 262 cases raising the same legal questions have been instituted and others are sure to follow. The United States further contends that its current interpretation of the statute and regulation is correct, even though it took the opposite position for nearly twenty years. As we demonstrate in this reply memorandum, these contentions are devoid of merit.

I. The Questions Presented Affect Hundreds Of Pending Cases And Many Millions of Dollars In Tax Liability Are Involved

The government's principal ground for opposing the petition is that, although there is a pervasive conflict among the Circuits, Congress has prospectively resolved the conflict and only "$6 million" in contested tax liabilities are affected by the questions presented. Opp. 5-6 & n. 4. However, as the government has conceded, there are now "administratively pending some 262 cases raising this issue." Pet. App. 62a. In addition, other cases are sure to be filed that are not yet in the litigation process. Thus, as explained by amicus American Gas Association, the instant case has "substantial continuing significance for a large number of taxpayers." Amicus Br. 3. It also has continuing significance for utility ratepayers: "The result has been to increase the amounts paid for utility gas service by all end-users, including approximately 41 million domestic residences served by A.G.A. membership." *Id.* at 2.

The hundreds of pending cases involve utilities across the United States and are destined to reach every federal Circuit. The district courts and courts of appeals, faced with this litigation, must attempt to grapple with numerous conflicting authorities. In a thoroughly reasoned opinion, the Ninth Circuit has decided the issue in favor of the taxpayer. *Pacific Gas & Electric Co.* v. *United States,* 664 F.2d 1133 (9th Cir. 1981). The Claims Court also has decided the issue in favor of the taxpayer. See *Minnesota Power and Light Co.* v. *United States,* 6 Cl. Ct. 558 (1984), *appeal pending before the Federal Circuit.* By contrast, the Seventh Circuit, over Judge Pell's vigorous dissent, has agreed with the government in the instant case. Pet. App. 1a-12a. The Eighth Circuit, relying on a district court decision later reversed by the Ninth Circuit, also has agreed with the government. *Northern States Power Co.* v. *United States,* 663 F.2d 55 (8th Cir. 1981), *cert. denied,* 456 U.S. 965 (1982).

Beyond this, the conflict in the lower courts has spread since the petition was filed, with inconsistent decisions handed down by district courts sitting in the Second and Eleventh Circuits. See *Alabama Power Co.* v. *United States,* ____ F. Supp. ____, 85-1 U.S.T.C. ¶ 16,432, No. 83-AR-3014-S (N.D. Ala. 1985) (resolving the legal question in favor of the taxpayer, but finding that the taxpayer failed to meet its factual burden of proof); *Consolidated Edison Co.* v. *United States,* ____ F. Supp. ____, 85-1 U.S.T.C. ¶ 16,431, No. 84 Civ. 1167 (S.D.N.Y. 1985), *appeal pending before the Second Circuit* (resolving the legal question in favor of the government).

In view of the conflicting lower court precedents, district courts and courts of appeals across the country have no escape from years of burdensome litigation, with the inevitable consequence of inconsistent rulings and differing tax liabilities depending solely on geography. Only this Court can efficiently and authoritatively settle this controversy for the Nation. This is precisely the situation in which the Court should grant certiorari — to ease the burden on lower federal courts and to restore uniformity to federal law.

Substantial revenue is at stake in this matter as well. Although the United States estimates that only $6 million in tax revenue is involved in the 262 currently pending cases (Opp. 6 n. 4), that estimate fails to include all of the open taxable years beyond those immediately at issue in pending litigation. In other words, the government's estimate fails to reflect all open taxable years prior to July 1, 1984 — taxable years which are subject to the conflicting case law but which are not all at the audit stage. For example, petitioner Northern Illinois Gas Company has $93,000 at stake for the three years covered by this case, but it also has 13 total open taxable years prior to July 1, 1984. Thus, referring only to the six cases that have produced published opinions which disclose the amounts at stake, but considering all open taxable years, those cases,

standing by themselves, involve approximately $2.5 million in revenue.[1] If these six cases are a representative sampling, then the total revenue at stake in the 262 pending cases would be approximately $100 million.

Accordingly, while it is true that Congress has *prospectively* settled this issue as of July 1, 1984, the issue continues to have substantial practical importance. As previously noted, petitioner has 13 open taxable years prior to July 1, 1984, and many other utility companies are in the same position. In the words of the American Gas Association, which represents 300 public utilities in all 50 states (Amicus Br. 2, 4) (emphasis supplied):

> "The conflict in these decisions is of vital importance to members of A.G.A. doing business in circuits where decisions have been rendered and to other members doing business within the other circuits which have not yet ruled on the issue but which may be influenced by the conflicting decisions. * * * The necessity for resolution of this conflict by this Court is also indicated by the substantial number of cases in which this issue is involved. * * * *The circuits are squarely in conflict on an important issue that affects nearly every utility.*"

This Court has not hesitated to grant certiorari in similar cases even when Congress has amended the tax laws on a prospective basis. For example, in *United States* v. *Chicago, Burlington & Quincy Railroad Co.*, 412 U.S. 401, 404 (1973), this Court reviewed a tax case even though there was no conflict among the Circuits because "the Court of Claims' decision apparently would afford a precedent for the tax treatment of substantial sums." The Court noted that, despite the prospec-

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[1] The $2.5 million figure is derived by adding the amounts the six taxpayers have at issue for all open taxable years prior to July 1, 1984. This computation is based on the assumption that the annual average tax liability for the taxable years in litigation equals the average annual tax liability for the remaining open taxable years.

tive change in the statute, large amounts of tax liability were "still litigable." *Id.* at 405 n. 6. The same is true here.

Congress clearly did not intend utility ratepayers in some sections of the country to bear a disproportionate share of the Highway Use Tax; nor did it intend to countenance conflicting constructions of the statute. In changing the law as of July 1, 1984, Congress expressly decided not to interfere with ongoing litigation for the many prior open taxable years. See Pet. 9 n. 3 (quoting the relevant statute and legislative history). Indeed, far from providing a ground for denying certiorari, Congress expressly stated that "no inference for past periods [is] to be drawn from [the 1983] amendment relating to customary use of trailers." *Ibid.* House Ways and Means Committee Chairman Rostenkowski stressed that "it was not the committee's intention to influence the outcome of ongoing litigation." *Ibid.* In view of the substantial volume of ongoing litigation, the large dollar amount at issue, the financial burden on public utilities across the country, the litigation burden on district courts and courts of appeals in every Circuit, and the discrepant tax liability in different sectors of the country, review by this Court at this time is plainly warranted.

II. The Seventh Circuit Has Seriously Misconstrued The Highway Use Tax Act

The lion's share of the government's brief in opposition is devoted to the argument that the "equipped for use" interpretation was established by Treasury Regulations promulgated in 1956, and that Revenue Ruling 76-294, 1976-2 C.B. 364, which applies the "equipped for use" test to utility trucks without regard to whether trailers are "customarily used" with such trucks, was not a change from prior law. Opp. 2-4. This argument is devoid of merit.

First, contrary to the government's assertion, the "customary use" test prescribed by the statute—and not the

"equipped for use" test—was adopted as the governing rule in the Treasury Regulations promulgated in 1956. The phrase "equipped for use" appeared only in a table which categorized various types of trucks; there is no evidence that the descriptive sentence fragments in that table were meant to displace the operative "customary use" test set forth in the Highway Use Tax Act and twice repeated in the text of the Treasury Regulations. See Pet. 2-3; Pet. App. 8a-9a, 27a-29a and 35a-40a. The United States' argument falls of its own weight once it is recognized that the "customary use" test was the governing test adopted in the statute and the 1956 Treasury Regulations. Moreover, the interpretation now proffered by the government would render the "customary use" criterion a nullity, contrary to accepted rules of statutory interpretation. See Pet. 10-11. Statutory language cannot be overridden in this fashion. *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 198-199 (1976).

Second, the government consistently applied the "customary use" test for over 20 years, despite its present assertion that the IRS did not "change" its position in 1976. Opp. 4-5 n.3. There are 13 published Revenue Rulings[2] and nine General Counsel Memoranda (GCMs)[3] dating from 1958 to 1978 which uniformly apply the "customary use" test in accordance with the following standard:

> "... in order to classify a particular vehicle as a taxable truck-trailer combination, there must first be an evidentiary finding that on a nationwide basis, trailers are customarily used with the type of truck in question; ... GCM 30742 (June 19, 1958) ... points out that while the words 'customarily used' with reference to semitrailers and trail-

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[2] Revenue Ruling 57-547, 1957-2 C.B. 789; Revenue Ruling 60-260, 1960-2 C.B. 347; Revenue Ruling 72-109, 1972-1 C.B. 351; Revenue Ruling 74-539, 1974-2 C.B. 376; Revenue Ruling 74-461, 1974-2 C.B. 377; Revenue Ruling 74-513, 1974-2 C.B. 377; Revenue Ruling 75-297, 1975-2 C.B. 443; Revenue Ruling 76-558, 1976-2 C.B. 360; Revenue Ruling 76-559, 1976-2 C.B. 365; Revenue Ruling 77-36, 1977-1 C.B. 347; Revenue Ruling 78-156, 1978-1 C.B. 365; Revenue Ruling 78-208, 1978-1 C.B. 366; Revenue Ruling 78-314, 1978-2 C.B. 269.

[3] The nine GCMs are listed at Pet. 4 n. 2.

> ers appear not [only] in sections 4481(a) and 4482(b), but also in Treas. Reg. § 41.4482(a)-1 and 41.4482(b)-1, the words 'equipped for use in combinations' appear only in the use tax schedule. The GCM concludes, therefore, that it must first be determined whether trailers are 'customarily used' with the type of truck in question. Only after that determination is made, is the use tax schedule consulted to determine the taxable gross weight." GCM 38962, *CCH IRS Positions* ¶ 1164 (February 16, 1983) (describing the prior practice of the IRS).

The lone inconsistent authority is Revenue Ruling 76-294, which applies an "equipped for use" presumption to utility trucks equipped with pintle hooks without regard to whether these trucks are "customarily used" with trailers.

The government also makes the incredible statement that the GCMs "did not accurately state IRS policy as set forth in the Commissioner's published rulings." Opp. 5 n.3. However, the 13 published Revenue Rulings, many of which were the subject of the nine GCMs, all apply the "customary use" test as described in the GCMs. And, as a matter of IRS practice, trucks equipped with trailer hitches were classified as truck-trailer combinations *only* where there was a finding of fact that such trucks customarily pull heavy trailers. Pet. App. 41a-49a.

Equally incredible is the government's assertion that "GCMs are not authoritative sources as to the administrative practice of the IRS." Opp. 5 n. 3. The nature of GCMs was analyzed thoroughly in *Taxation With Representation Fund* v. *IRS*, 646 F.2d 666, 682 (D.C. Cir. 1981), in which the court concluded that:

> "In essence, after a decision has been reached, a completed GCM becomes an expression of agency policy * * *. GCMs function as a body of 'working law' within the IRS."

The nine GCMs and 13 published Revenue Rulings cannot be dismissed as a passing curiosity. They clearly establish that

the government adopted and consistently applied the "customary use" test from 1956 to 1976, and that the "equipped for use" test of Revenue Ruling 76-294 was a fundamental change in the application of the Highway Use Tax Act. As the Claims Court recently explained (Pet. App. 49a-50a):

> "the statutes and the regulations, adopted in 1956, expressly incorporate the statutory 'customary use' standard, and both the revenue rulings and the GCMs, commencing in 1957 and continuing for nearly 20 years, uniformly enunciate the same 'customary use' standard. These revenue rulings and GCMs constitute a 'substantially contemporaneous construction of the statute by those presumed to have been aware of congressional intent' and are entitled to particular force. *Corn Products Refining Co.* v. *Commissioner*, 350 U.S. 46, 52-53 (1955) (longstanding Treasury position in a published GCM given deference)."

Third, contrary to the government's assertion that "the Commissioner may correct an earlier position" (Opp. 5 n. 3), reversal of a legislative rule can be effected only in accordance with the Administrative Procedure Act. See Pet. 12-16. The government's assertion that Revenue Ruling 76-294 was merely "an interpretive [sic] ruling" (Opp. 2 and 6) is clearly wrong because Revenue Ruling 76-294 dramatically changed prior law by adopting the "equipped for use" rule without regard to the "customary use" of the vehicles involved.

Fourth, there is no merit to the government's hyperbolic statement that the "nationwide truck-by-truck factual investigation upon which petitioner insists would make the highway use tax virtually inadministrable." Opp. 4. If petitioner's construction is not a reasonably practicable one, then why, for twenty years, did the IRS and Treasury Department uniformly espouse it? Moreover, as the Claims Court recently explained, there is no substance to the administrative burden argument because it ignores the fact that the taxpayer, not the government, has the burden of proof (Pet. App. 59a):

> "although the Government raises the Pandora's box 'horror' of a trial on the merits of 'customary use,' both in this case and in a potential avalanche of cases still administratively pending, it must be noted that its assessment is presumptively correct, and it is the taxpayer, not the Government, who must carry the burden of proving that its vehicles are not of the type which the Government considers them to be. If the taxpayer is unable to prove that its vehicles are not of a type customarily used in combination with a trailer, then the assessment of additional highway use taxes will be upheld."

In this case, petitioner sustained its burden of proof by adducing accurate survey evidence establishing that the trucks at issue only infrequently pulled trailers on the public highways. Pet. 2 n. 1 and Pet. App. 10a.

Finally, the government's proffered interpretation vitiates the fundamental purpose of the Highway Use Tax Act, as it was in effect from 1956 to 1984. The Highway Use Tax was intended to fall heaviest on those that use the highways most. As Judge Pell explained in his dissent below (Pet. App. 9a-10a):

> "the intent of Congress was that the highway use tax bear most heavily on those whose use of the highway caused the most wear and tear. Imposing the tax on those types of trucks that are customarily used with heavy trailers is a reasonable method of determining which types of trucks should bear the burden of the tax. The customary-use test is not a fine-tuned means of apportioning the burden of the use tax, but it is related to the actual use of the highways by a type of truck. The equipped-for-use test, in contrast, is inconsistent with Congress' attempt to apportion the tax equitably. The equipped-for-use test is not reflective of the actual use of the heavy trailer. A pintle hook, by itself, causes no additional wear on a highway. As the evidence appellant attempted to introduce demonstrates, utility trucks equipped with pintle hooks more often than not are *not* used in combination with heavy trailers."

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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